Directors Beware
The Taxman Cometh – Again !!!

October 2011

As you may have already heard, tucked away in the 2011 Federal Budget were proposed changes to the ATO's ability to make claims against directors of companies for not only unnpaid PAYG but also unpaid employee superannuation. Whilst the charges have been earmarked as "Anti Phoenix" legislation, in reality they have broad consequesces for any director whose company is behind on payments of either PAYG or employee superannuation.

Director Penalty Notices have been around since 1993, however the changes substantially alter:

- The amounts claimable against a director under the "Director Penalty" regime to now include both unpaid PAYG and employee superannuation; and
- The concept of 21 days Notification of a Director Penalty Notice by the ATO overruled by the **automatic liability** trigger in certain circumstances.

The changes are simply summarised by the following table which is taken from the explanatory memorandum to the draft changes in Legislation.

Current law	***New law***
Directors are peronally liabile for their company's unpaid PAYG withholding amounts after the expiry of an issued Directors Penalty Notice (DPN).	In addition to liability for PAYG withholding amounts, directors are personally liable for their company's unpaid Superannuation Guarantee Charge amounts.
An estimate can only be raised by the ATO in relation to PAYG Withholding liabilities.	In addition to estimating unpaid PAYG withholding liabilities, the Commissioner can estimate a Superannuation Guarantee Charge debt.
For arrears PAYG the Commissioner may issue a Director Penalty Notice and may only commence recovery against the director 21 days after the notice was issued. A director can extinguish their personal liabillity by causing one of three things to happen within that 21 day notice period: • payment of the debt; • appointment of an adminstrator under section 436A, 436B or 436C of the corporations Act 2001; or • beginning the winding up of the company.	The current law continues to apply where a company's debt to which the director penalty applies is less than three months older where the debt has been correctly reported before three months from the due day passes. In these circumstancs director liability occurs after the service and expiry of a DPN notice. Once the company's "unreported debt" is three months old, the Commissioner can commence proceedings to recovery the penalty immediately and, a director's personal liability is only extinguished by payment of the debt or penalty

Regardless of whether a company has paid PAYG withholding amounts to the Commissioner, its directors like all other company employees are entitled to PAYG withholding credits withheld by the company from a withholding payment made to the director.	Where a company has failed to pay PAYG withholding amounts to the Commissioner, the Commissioner has a discretion to reduce a director's entitlement to PAYG withholding credits relating to withholding payments made from the company . They will therefore be personally liable for any tax due
A company director's associates are entitled to PAYG withholding credits withheld by the company from a withholding payment made to the associate, such as salary, regardless of whether the company has paid the PAYG withholding amounts to the Commissioner.	Where a company has failed to pay PAYG withholding amounts to the Commissioner, the Commissioner has a discretion to reduce the creditors associate that relate to withholding payment made from the company.

The key issues from the abve table are as follows:

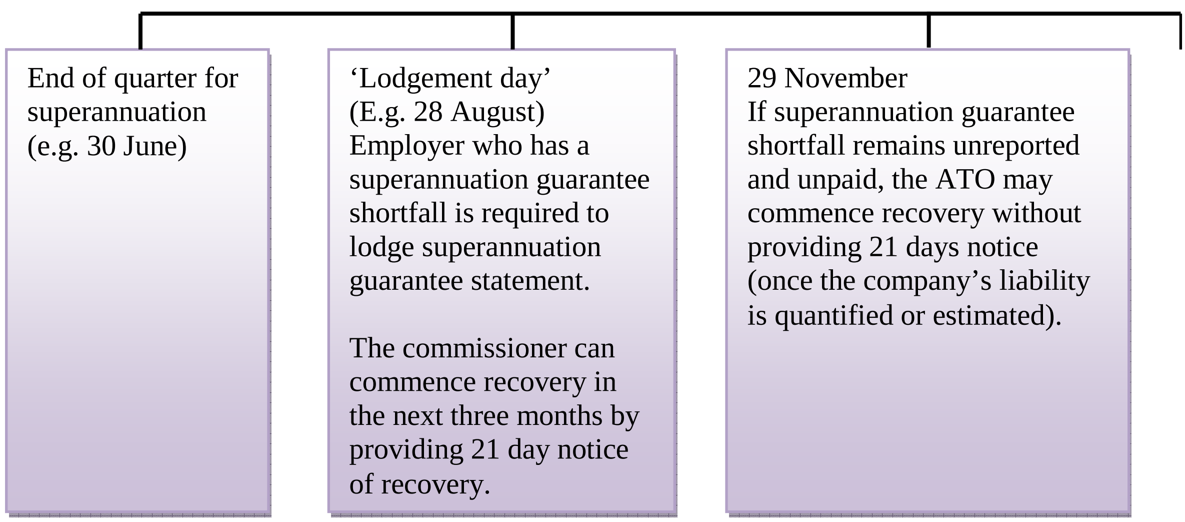
<u>Reporting as opposed to Payment.</u>

There is a distinction in the legislative intent between "*Reporting a Liability*" and "*Payment of a liability*". If the relevant lodgements are undertaken, as and when reqiured, to report a liability as being due, buy obviously not paid, then the OLD Director Penalty Notice regime applies and diretors will still have 21 days in which to remedy the position after the service of a DPN.

If a liability is "unreported", after 3 months of when they were required then an automatice liability for the debts crystallises against the directors of the company.

It is therefore important to ensure that all relevant returns are lodged by the due date even if without payment. Whilst this will not stop the issuance of a DPN with a 21 day action period it will prevent the use of the automatic liability provisions.

They say a picture is worth a thousand words so see the following as an example preovided by the Explanatory Memorandum.



No Credit for unpaid PAYG on Directors Returns.

These new provisions provide a discretion on the part of the ATO to reduce a directors entitlement to PAYG withholding credits in their personal returns where a company has failed to remit the relevant taxes. This is also capable of being used against "Associates" of the director.
Whilst the language of the explanatory memorandum is in terms of "Phoenix" activites it remains to be seen just how broadly these new provisions are applied.

When do the provisions apply from

Whilst the Budget papers made reference to the Law being effective from the 1st July 2011 the Explantory Memorandum states:

1). The automated DPN provisions *"will apply to all director penalties that are due and payable at or after commencement of these amendments on the day after* Royal Assent of the Bill".
2). The automated DPN provisions also apply to director penalties in existence before the commencement of new provisions if those penalties were not extinguisehed before the commencement. To extinguish you must have either paid the penalty or appointed a Liquidator or Voluntary Adminstrator to the company.
3). The Superannuation Guarantee Charge liability apply if the company is required to lodge a quarterly superannuation guarantee statemen to report unpaid and overdue super guarantee shortfall on or after the day on which the amendments commence (i.e. No substantive retrospectivity.
4). The reduction of credits to directors for unpaid PAYG applies from the 2011 – 2012 income year.

The consultation period for draft legislation has now expired. As to when the legislation will be introduced into Parliament, which starts the process of obtaining "Royal Assent" is unknow however you should assume it will be sooner rather than later.

Where to from here?

If you are a director and your company is currently having difficulties meeting its obligations in relation to PAYG Withholding and Superannuation Guarantee; make sure that all lodgement obligations are currently up-to-date even if you are unable to meet payment of these obligations by the due dates. When your company is unable to meet payment obligations by their due dates, don't just bury your head in the sand and hope for the best, get in contact with your tax agent or the ATO to come to an arrangement prior to the ATO taking it upon themselves to calculate any outstanding liability, issusing a Directors Penalty Notice and comencing recovery action that you may be personally liable.